

## TOPIC – 3

### ACCOUNTING STANDARD – 2

### VALUATION OF INVENTORIES

### Total No. of Questions - 18

#### Q.AS2.RMP.01 (RTP N23)

Alpha Ltd. sells flavored milk to customers; some of the customers consume the milk in the shop run by Alpha Limited. While leaving the shop, the consumers leave the empty bottles in the shop and the company takes possession of these empty bottles. The company has laid down a detailed internal record procedure for accounting for these empty bottles which are sold by the company by calling for tenders.



Keeping this in view:

Decide whether the inventory of empty bottles is an asset of the company;

If so, whether the inventory of empty bottles existing as on the date of Balance Sheet is to be considered as inventories of the company and valued as per AS 2 or to be treated as scrap and shown at realizable value with corresponding credit to 'Other Income'?

#### Q.AS2.SM.02: (MTP May21& May22)

In a production process, normal waste is 5% of input. 5,000 MT of input were put in process resulting in wastage of 300 MT. Cost per MT of input is Rs 1,000. The entire quantity of waste is on stock at the year end. State with reference to Accounting Standard, how will you value the inventories in this case?

#### Q.AS2.RMP.03: (EXAM May19)

Wooden Plywood Limited has a normal wastage of 5% in the production process. During the year 2017-18, the Company used 16,000 MT of Raw material costing Rs. 190 per MT. At the end of the year, 950 MT of wastage was in stock. The accountant wants to know how this wastage is to be treated in the books.

You are required to:

(1) Calculate the amount of abnormal loss.

(2) Explain the treatment of normal loss and abnormal loss. [In the context of AS-2 (Revised)]

#### Q.AS2.SM.04: (MTP Nov19)

Mr. Mehl gives the following information relating to items forming part of inventory as on 31-3-2015. His factory produces Product X using Raw material A.

(i) 600 units of Raw material A (purchased @ Rs. 120). Replacement cost of raw material A as on 31-

3-2015 is Rs. 90 per unit.

- (ii) 500 units of partly finished goods in the process of producing X and cost incurred till date Rs. 260 per unit. These units can be finished next year by incurring additional cost of Rs. 60 per unit.
- (iii) 1500 units of finished Product X and total cost incurred Rs. 320 per unit. Expected selling price of Product X is Rs. 300 per unit.

Determine how each item of inventory will be valued as on 31-3-2015. Also calculate the value of total inventory as on 31-3-2015.

### **Q.AS2.SM.05: (also RTP Nov.22)**

The closing inventory at cost of a company amounted to Rs. 2,84,700. The following items were included at cost in the total:



- (a) 400 coats, which had cost Rs. 80 each and normally sold for Rs. 150 each. Owing to a defect in manufacture, they were all sold after the balance sheet date at 50% of their normal price. Selling expenses amounted to 5% of the proceeds.
- (b) 800 skirts, which had cost Rs. 20 each. These too were found to be defective. Remedial work in April cost Rs. 5 per skirt, and selling expenses for the batch totaled Rs. 800. They were sold for Rs. 28 each.

What should the inventory value be according to AS 2 after considering the above items?

### **Q.AS2.OM.06: (CA Final)**

Mars Fashions is a new luxury retail company located in Lajpat Nagar, New Delhi. Kindly advise the accountant of the company on the necessary accounting treatment for the following items:



(a) One of Company's product lines is beauty products, particularly cosmetics such as lipsticks, moisturizers and compact make-up kits. The company sells hundreds of different brands of these products. Each product is quite similar, is purchased at similar prices and has a short lifecycle before a new similar product is introduced. The point of sale and inventory system is not yet fully functioning in this department. The sales manager of the cosmetic department is unsure of the cost of each product but is confident of the selling price and has reliably informed us that the Company, on average, make a gross margin of 65% on each line.

(b) Mars Fashions also sells handbags. The Company manufactures their own handbags as they wish to be assured of the quality and craftsmanship which goes into each handbag. The handbags are manufactured in India in the head office factory which has made handbags for the last fifty years. Normally, Mars manufactures 100,000 handbags a year in their handbag division which uses 15% of the space and overheads of the head office factory. The division employs ten people and is seen as being an efficient division within the overall company.

In accordance with AS 2, explain how the items referred to in a) and b) should be measured.

**Q.AS2.OM.07: (CA Final)**

In a manufacturing process of Mars Ltd, one by-product BP emerges besides two main products MPI and MP2 apart from scrap. Details of cost of production process are here under:



Item	Unit	Amount	Output	Closing Stock 31-3-20X1
Raw material	14,500	1,50,000	MP I-5,000 units	250
Wages	-	90,000	MP II - 4,000 units	100
Fixed overhead	-	65,000	BP- 2,000 units	-
Variable overhead	-	50,000	-	-

Average market price of MPI and MP2 is Rs. 60 per unit and Rs. 50 per unit respectively, by-product is sold @ Rs. 20 per unit. There is a profit of Rs. 5,000 on sale of by-product after incurring separate processing charges of Rs. 8,000 and packing charges of Rs. 2,000, Rs. 5,000 was realised from sale of scrap.

**Required:**

Calculate the value of closing stock of MPI and MP2 as on 31-03-20X1.

**Q.AS2.RMP.08: (RTP May18)**

A private limited company manufacturing fancy terry towels had valued its closing inventory of inventories of finished goods at the realizable value, inclusive of profit and the export cash incentives. Firm contracts had been received and goods were packed for export, but the ownership in these goods had not been transferred to the foreign buyers. You are required to advise the company on the valuation of the inventories in line with the provisions of AS 2.

**Q.AS2.RMP.09: (RTP Nov18)**

A Limited is engaged in manufacturing of Chemical Y for which Raw Material X is required. The company provides you following information for the year ended 31<sup>st</sup> March, 2017.

	Rs Per unit
<b>Raw Material X</b>	
Cost price	380
Unloading Charges	20
Freight Inward	40
Replacement cost	300
<b>Chemical Y</b>	
Material consumed	440
Direct Labour	120
Variable Overheads	80
Fixed Overheads	20

**Additional Information:**

(i) Total fixed overhead for the year was Rs. 4,00,000 on normal capacity of 20,000 units.

(ii) Closing balance of Raw Material X was 1,000 units and Chemical Y was Rs. 2,400 units.

You are required to calculate the total value of closing stock of Raw Material X and Chemical Y according to AS 2, when

(i) Net realizable value of Chemical Y is Rs. 800 per unit

(ii) Net realizable value of Chemical Y is Rs. 600 per unit

**Q.AS2.RMP.10: (RTP May20)**

Particulars		Kg.	Rs
Opening Inventory:	Finished Goods	1,000	25,000
	Raw Materials	1,100	11,000
Purchases of Raw Material		10,000	1,00,000
Labour			76,500
Overheads (Fixed)			75,000
Sales		10,000	2,80,000
Closing Inventory:	Raw Materials	900	
	Finished Goods	1200	



The expected production for the year was 15,000 kg of the finished product. Due to fall in market demand the sales price for the finished goods was Rs. 20 per kg and the replacement cost for the raw material was Rs. 9.50 per kg on the closing day. You are required to calculate the closing inventory as on that date.

**Q.AS2.RMP.11: (RTP May21)**

The inventory of Rich Ltd. as on 31<sup>st</sup> March, 2020 comprises of Product – A: 200 units and Product – B: 800 units.

Details of cost for these products are:

Product – A: Material cost, wages cost and overhead cost of each unit are Rs. 40, Rs. 30 and Rs. 20 respectively, Each, unit is sold at Rs. 110, selling expenses amounts to 10% of selling costs.

Product – B: Material cost and wages cost of each unit are Rs. 45 and Rs. 35 respectively and normal selling rate is Rs. 150 each, however due to defect in the manufacturing process 800 units of Product-B were expected to be sold at Rs. 70.

You are requested to value closing inventory according to AS 2 after considering the above.

**Q.AS2.RMP.12: (MTP Nov21)**

From the following information provided by XYZ Limited you are required to compute the closing inventory:

**Raw Material P**

Closing balance	600 units
	Rs. per unit
Cost price including GST	250
Input tax credit available	20
Freight inward	30
Handling charges	15
Replacement cost	180

**Finished goods Q**

Closing balance	1,500 units
	Rs. per unit
Material consumed	250
Direct labour	70
Direct overhead	30

Total fixed overhead for the year was Rs. 3,00,000 on a normal capacity of 30,000 units while actual production has been of 25,000 units.

Calculate the value of closing stock, when

- (i) Net realizable value of the finished good Q is Rs. 450 per unit.  
 (ii) Net Realizable value of the Finished Good Q is Rs. 340 per unit.

### **Q.AS2.SM.13:**

Venus Trading Company purchases cars from several countries and sells them to Asian countries. During the current year, this company has incurred following expenses:

1. Trade discounts on purchase
2. Handling costs relating to imports
3. Salaries of accounting department
4. Sales commission paid to sales agents
5. After sales warranty costs
6. Import duties
7. Costs of purchases (based on supplier's invoices)
8. Freight expense
9. Insurance of purchases
10. Brokerage commission paid to indenting agents

Evaluate which costs are allowed by AS 2 for inclusion in the cost of inventory in the books of Venus.

### **Q.AS2.SM.14: (RTP Also)**

X Co. Limited purchased goods at the cost of Rs 40 lakhs in October, 2016. Till March, 2017, 75% of the stocks were sold. The company wants to disclose closing stock at Rs 10 lakhs. The expected sale value is Rs 11 lakhs and a commission at 10% on sale is payable to the agent. Advice, what is the correct closing stock to be disclosed as at 31.3.2017.

### **Q.AS2.RMP.15: (RTP May23)**

An enterprise ordered 20,000 KG of certain material at ₹ 110 per unit. The purchase price includes GST ₹ 12 per KG, in respect of which full input tax credit (ITC) is admissible. Freight incurred amounted to ₹ 1,17,600. Normal transit loss is 2%. The enterprise actually received 19,500 KG and consumed 18,000 KG of the material.

- (i) You are required to calculate cost of material per KG;  
 (ii) Allocation of material cost.

**Q.AS2.RMP.16: (EXAM Nov22)**

Following information of Sarah Limited is given:

Sarah Limited uses Raw Material 'A' for production of production of Finished Goods 'B'



Closing balance of Raw Material 'A' in units on 31st March, 2022	750
	<b>Price Per Unit in ₹</b>
Cost Price	150
Freight inward	10
Replacement Cost	152
Closing balance of Finished Good 'B' in units on 31st March, 2022	1,600
	<b>Price Per Unit in ₹</b>
Material Consumed	225
Direct Labour	75
Direct variable overhead	60

Total Fixed Overheads amounts to ₹ 1,00,000 on normal capacity of 20,000 units.

You are required to calculate the value of Closing Stock of Raw materials and Closing Stock of Finished Goods, as on 31st March, 2022, as per AS 2, when selling price of Finished Goods 'B' is ₹ 360 per unit.

**Q.AS2.SM.17:**

You are required to value the inventory per kg of finished goods consisting of:

	Rs per kg.
Material cost	200
Direct labour	40
Direct variable overhead	20



Fixed production charges for the year on normal working capacity of 2 lakh kgs is Rs 20 lakhs. 4,000 kgs of finished goods are in stock at the year end.

**Q.AS2.RMP.18: (RTP May22)**

(a) "In determining the cost of inventories, it is appropriate to exclude certain costs and recognize them as expenses in the period in which they are incurred". Provide examples of such costs as per AS 2 'Valuation of Inventories'.

(b) Rohan Pvt. Ltd., a wholesaler in agriculture products, has valued the inventory on Net Realizable Value on the ground that AS 2 does not apply to inventory of agriculture products.



## SOLUTIONS OF ABOVE QUESTIONS

### SOLUTION OF Q1

As per the 'Framework on Presentation and Preparation of Financial Statements':

Tangible objects or intangible rights carrying probable future benefits, owned by an enterprise are called assets.

Alpha Ltd. sells these empty bottles by calling tenders. It means further benefits are accrued on its sale.

Therefore, empty bottles are assets for the company.

As per AS 2, inventories are assets held for sale in the ordinary course of business.

Inventory of empty bottles existing on the Balance Sheet date is the inventory and Alpha Ltd. has detailed controlled recording and accounting procedure which duly signify its materiality.

Thus, inventory of empty bottles cannot be considered as scrap and should be valued as inventory in accordance with AS 2.

### Solution Q2

As per AS 2 (Revised), abnormal amounts of wasted materials, labour and other production costs are excluded from cost of inventories and such costs are recognised as expenses in the period in which they are incurred.

In this case, normal waste is 250 MT and abnormal waste is 50 MT. The cost of 250 MT will be included in determining the cost of inventories (finished goods) at the year end. The cost of abnormal waste (50 MT x 1,052.6315 = Rs 52,632) will be charged to the profit and loss statement.

Cost per MT (Normal Quantity of 4,750 MT) = 50,00,000 / 4,750 = Rs 1,052.6315

Total value of inventory = 4,700 MT x Rs 1,052.6315 = Rs 49,47,368.

### SOLUTION Q3

1. As per AS 2 (Revised) 'Valuation of Inventories', abnormal amounts of wasted materials, labour and other production costs are excluded from cost of inventories and such costs are recognised as expenses in the period in which they are incurred. The normal loss will be included in determining the cost of inventories (finished goods) at the year end.

#### 2. Amount of Abnormal Loss:

Material used 16,000 MT @ Rs. 190	Rs. 30,40,000
Normal Loss (5% of 16,000 MT) (included in calculation of cost of inventories)	800 MT
Net quantity of material	15,200 MT

(iii) Abnormal Loss in quantity (950 - 800) 150 MT

Abnormal Loss Rs. 30,000

[150 units @ Rs. 200 (Rs. 30,40,000/15,200)]

Amount of Rs. 30,000 (Abnormal loss) will be charged to the Profit and Loss

### SOLUTION Q4

As per AS 2 "Valuation of Inventories", materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at cost or above cost. However, when there has been a decline in the price of materials and it is estimated that the cost of the finished products will exceed net realizable value, the materials are written down to net realizable value. In such circumstances, the replacement cost of the

materials may be the best available measure of their net realizable value. In the given case, selling price of product X is Rs. 300 and total cost per unit for production is Rs. 320.

Hence the valuation will be done as under:

- (i) 600 units of raw material will be written down to replacement cost as market value of finished product is less than its cost, hence valued at Rs. 90 per unit.
- (ii) 500 units of partly finished goods will be valued at 240 per unit i.e., lower of cost Rs. 320 (Rs. 260 + additional cost Rs. 60) or Net estimated selling price Rs. 240 (Estimated selling price Rs. 300 per unit less additional cost of Rs. 60).
- (iii) 1,500 units of finished product X will be valued at NRV of Rs. 300 per unit since it is lower than cost Rs. 320 of product X.

Valuation of Total Inventory as on 31.03.2015:

	Units	Cost (Rs.)	NRV/Replacement cost	Value = units x cost or NRV whichever is less (Rs.)
Raw material A	600	120	90	54,000
Partly finished goods	500	260	240	1,20,000
Finished goods X	1,500	320	300	4,50,000
<b>Value of Inventory</b>				<b>6,24,000</b>

### SOLUTION Q5

#### Valuation of Closing Stock

Particulars	Rs.	Rs.
Closing Stock at cost		2,84,700
Less: adjustment required for 400 defected coats		3,500
Cost of 400 coats (400 x 80)	32,000	
Net Realisable Value [400 x (75 - 5% of Rs. 75)]	28,500	
(400 coats should be measured at NRV which is lower i.e. 28,500 therefore adjustment of 3500 is required)		
<b>Value of Closing Stock</b>		<b>2,81,200</b>

Note: There is no adjustment for skirts because for skirts were sold at above cost.

### SOLUTION Q6

(a) The retail method can be used for measuring inventories of the beauty products. The cost of the inventory is determined by taking the selling price of the cosmetics and reducing it by the gross margin of 65% to arrive at the cost.

(b) The handbags can be measured using standard cost especially if the results approximate cost. Given that the company has the information reliably on hand in relation to direct materials, direct labour, direct expenses and overheads, it would be the best method to use to arrive at the cost of inventories.

### Solution Q7

As per Ind 2 'Inventories', most by-products as well as scrap or waste materials, by their nature, are immaterial. They are often measured at net realizable value and this value is deducted from the cost of the main product.

#### 1) Calculation of NRV of By-product BP

Selling price of by-product	2,000 units x 20 per unit	40,000
Less: Separate processing charges of by-product BP		(8,000)
Packing charges		(2,000)
<b>Net realizable value of by-product BP</b>		<b>30,000</b>

## 2) Calculation of cost of conversion for allocation between joint products MP1 and MP2

Raw material		1,50,000
Wages		90,000
Fixed overhead		65,000
Variable overhead		50,000
Less: NRV of by-product BP (See Calculation 1)	30,000	
Sale value of scrap	5,000	(35,000)
<b>Joint cost to be allocated between MP1 and MP2</b>		<b>3,20,000</b>

## 3) Determination of "basis for allocation" and allocation of joint cost to MP1 and MP2

	<b>MP 1</b>	<b>MP 2</b>
Output in units (a)	5,000	4,000
Sales price per unit (b)	60	50
Sales value (a x b)	3,00,000	2,00,000
Ratio of allocation	3	2
Joint cost of Rs. 3,20,000 allocated in the ratio of 3:2 (c)	1,92,000	1,28,000
<b>Cost per unit [C/A]</b>	<b>38.4</b>	<b>32</b>

## 4) Determination of Value of Closing stock of MP 1 &amp; MP 2

<b>Particulars</b>	<b>MP 1</b>	<b>MP 2</b>
Closing stock in units	250 units	100 units
Cost per unit	38.4	32
Value of closing stock	9,600	3,200

**SOLUTION Q8**

Accounting Standard 2 "Valuation of Inventories" states that inventories should be valued at lower of historical cost and net realizable value. The standard states, "at certain stages in specific industries, such as when agricultural crops have been harvested or mineral ores have been extracted, performance may be substantially complete prior to the execution of the transaction generating revenue. In such cases, when sale is assured under forward contract or a government guarantee or when market exists and there is a negligible risk of failure to sell, the goods are often valued at net realizable value at certain stages of production."

Terry Towels do not fall in the category of agricultural crops or mineral ores. Accordingly, taking into account the facts stated, the closing inventory of finished goods (Fancy terry towel) should have been valued at lower of cost and net realizable value and not at net realizable value. Further, export incentives are recorded only in the year the export sale takes place. Therefore, the policy adopted by the company for valuing its closing inventory of inventories of finished goods is not correct.

**SOLUTION Q9**

## (i) When Net Realizable Value of the Chemical Y is Rs. 800 per unit

NRV is greater than the cost of Finished Goods Y i.e., Rs 660 (Refer W.N.) Hence, Raw Material and Finished Goods are to be valued at cost.

Value of Closing Stock:

	Qty.	Rate (Rs)	Amount (Rs)
Raw Material X	1,000	440	4,40,000
Finished Goods Y	2,400	660	15,84,000
<b>Total Value of Closing Stock</b>			<b>20,24,000</b>

## (ii) When Net Realizable Value of the Chemical Y is Rs 600 per unit

NRV is less than the cost of Finished Goods Y i.e., Rs. 660. Hence, Raw Material is to be valued at replacement cost and Finished Goods are to be valued at NRV since NRV is less than the cost.

Value of Closing Stock:

	Qty.	Rate (Rs)	Amount (Rs)
Raw Material X	1,000	300	3,00,000
Finished Goods Y	2,400	600	14,40,000

Total Value of Closing Stock			<u>17,40,000</u>
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**Working Note:****Statement showing cost calculation of Raw material X and Chemical Y**

<b>Raw Material X</b>	<b>Rs</b>
Cost Price	380
Add: Freight Inward	40
Unloading charges	<u>20</u>
Cost	<u>440</u>
<b>Chemical Y</b>	<b>Rs</b>
Materials consumed	440
Direct Labour	120
Variable overheads	80
Fixed overheads (Rs 4,00,000/20,000 units)	<u>20</u>
Cost	<u>660</u>

**SOLUTION Q10****Calculation of cost for closing inventory**

<b>Particulars</b>	<b>Rs</b>
Cost of Purchase (10,200 x 10)	1,02,000
Direct Labour	76,500
Fixed Overhead $75,000 \times 10,200 / 15,000$	51,000
Cost of Production	<u>2,29,500</u>
Cost of closing inventory per unit (2,29,500/10,200)	Rs 22.50
Net Realisable Value per unit	Rs 20.00

Since net realisable value is less than cost, closing inventory will be valued at Rs. 20.

As NRV of the finished goods is less than its cost, relevant raw materials will be valued at replacement cost i.e. Rs. 9.50.

Therefore, value of closing inventory: Finished Goods (1,200 x 20) Rs. 24,000

Raw Materials (900 x 9.50) =Rs. 8,550

Total =Rs. 32,550

**SOLUTION Q11**

According to AS 2 'Valuation of Inventories', inventories should be valued at the lower of cost and net realizable value.

**Product - A**

Material cost	Rs. 40 x 200 = 8,000	
Wages cost	Rs. 30 x 200 = 6,000	
Overhead	Rs. 20 x 200 = <u>4,000</u>	
Total cost		Rs. 18,000
Realizable value [200 x (110-11)]		Rs. 19,800
Hence inventory value of Product -A		Rs. 18,000

**Product - B**

Material cost	Rs. 45 x 800 = 36,000	
Wages cost	Rs. 35 x 800 = <u>28,000</u>	
Total cost		Rs. 64,000
Realizable value (800 x 70)		Rs. 56,000
Hence inventory value of Product-B		Rs. 56,000
Total Value of closing inventory i.e. Product A + Product B (18,000+ 56,000)		Rs. 74,000

**SOLUTION Q12**

(i) When Net Realizable Value of the Finished Good Q is Rs. 450 per unit Value of Closing Stock:

	Valuation Base	Qty.	Rate (Rs.)	Amount (Rs.)
Raw Material P	Cost	600	275	1,65,000
Finished Good Q	Cost	1,500	360	5,40,000
Total value of closing stock				7,05,000

(ii) When Net Realizable Value of the Finished Good Q is Rs. 340 per unit  
Since NRV of finished goods Q is less than its cost i.e. Rs. 360 (Refer W.N.), raw material P is to be valued at replacement cost and finished goods is to be valued at NRV.

Value of Closing Stock:

	Valuation Base	Qty.	Rate (Rs.)	Amount (Rs.)
Raw material P	Replacement cost	600	180	1,08,000
Finished good Q	Net Realisable Value	1,500	340	5,10,000
Total value of closing stock				6,18,000

**Working Note:**

Statement showing calculation of cost of raw material P and finished good Q

<b>Raw Material P</b>	<b>Rs.</b>
Cost Price (250-20)	230
Add: Freight Inward	30
Handling charges	15
Cost	275
<b>Finished Goods Q</b>	<b>Rs.</b>
Materials consumed	250
Direct Labour	70
Variable overheads	30
Fixed overheads (Rs. 3,00,000 / 30,000 units)	10
	360

**Solution Q13**

Items number 1, 2, 6, 7, 8, 9, 10 are allowed by AS 2 for the Calculation of cost of inventories. Salaries of accounts department, sales commission, and after sale warranty costs are not considered to be the cost of inventory therefore, they are not allowed by AS 2 for inclusion in cost of inventory and are expensed off in the profit and loss account.

**Solution Q14**

As per AS 2 (Revised) "Valuation of Inventories", the inventories are to be valued at lower of cost or net realisable value.

In this case, the cost of inventory is Rs 10 lakhs. The net realisable value is  $11,00,000 \times 90\% = \text{Rs. } 9,90,000$ . So, the stock should be valued at Rs 9,90,000.

**Solution Q15**

Calculation of Normal cost per Kg.

	₹
Purchase price (20,000 Kg. x ₹ 110)	22,00,000
Less: Input Tax Credit (20,000 Kg. x ₹ 12)	(2,40,000)
	19,60,000

Add: Freight	1,17,600
A. Total material cost	20,77,600
B. Number of units normally received = 98% of 20,000 Kg.	Kg. 19,600
C. Normal cost per Kg. (A/B)	106

**Allocation of material cost**

	Kg.	₹/Kg.	₹
Materials consumed	18,000	106	19,08,000
Cost of inventory	1,500	106	1,59,000
Abnormal loss	100	106	10,600
Total material cost	19,600	106	20,77,600

Note: Abnormal losses are recognized as separate expense.

**SOLUTION Q16**

<b>Raw Material A</b>	₹
Cost Price	150
Add: Freight Inward	10
Cost per unit	160
Replacement cost per unit of raw material	152

As per AS 2 (Revised) "Valuation of Inventories", the inventories are to be valued at lower of cost or net realizable value. Materials and other supplies held for use in the production of inventories are written down below cost if the selling price of finished product containing the material does not exceed the cost of the finished product. In the given case, net realizable value of the Product 'B' (Finished Goods) is ₹ 360 per unit which is less than its cost ₹ 365 per unit. Raw Material is to be valued at replacement cost. Value of the closing stock of raw material on 31/03/2022 would be ₹ 1,14,000 (750 units X ₹152 per unit).

<b>Finished Goods B</b>	₹
Materials consumed	225
Direct Labour	75
Direct Variable overheads	60
Fixed overheads (₹ 1,00,000/20,000 units)	5
Cost per unit	365
Net realizable value per unit	360

As per AS 2 (Revised) "Valuation of Inventories", the inventories are to be valued at lower of cost or net realizable value. Hence, Finished Goods are to be valued at NRV since NRV is less than the cost. Value of the closing stock of Finished goods as on 31/03/2022 would be ₹ 5,76,000 (1,600 units X ₹ 360 per unit).

**Solution Q17**

In accordance with AS 2 (Revised), the cost of conversion includes a systematic allocation of fixed and variable overheads that are incurred in converting materials into finished goods. The allocation of fixed overheads for the purpose of their inclusion in the cost of conversion is based on normal capacity of the production facilities.

Cost per kg. of finished goods:

	Rs	
Material Cost		200
Direct Labour	40	
Direct Variable Production Overhead	20	
Fixed Production Overhead (2000000/200000)	10	70
		<u>270</u>

Hence the value of 4,000 kgs. of finished goods = 4,000 kgs x Rs 270 = Rs 10,80,000

### **SOLUTION Q18**

- (a) As per AS 2 "Valuation of Inventories", certain costs are excluded from the cost of the inventories and are recognised as expenses in the period in which incurred. Examples of such costs are: (a) abnormal amount of wasted materials, labour, or other production costs; (b) storage costs, unless those costs are necessary in the production process prior to a further production stage; (c) administrative overheads that do not contribute to bringing the inventories to their present location and condition; and (d) selling and distribution costs.
- (b) AS 2 does not apply to producers of agricultural products but applies to traders in agricultural products. Hence AS 2 will apply to Rohan Pvt. Ltd. and it will have to value inventory at lower of cost or market value.



Student Notes: -